

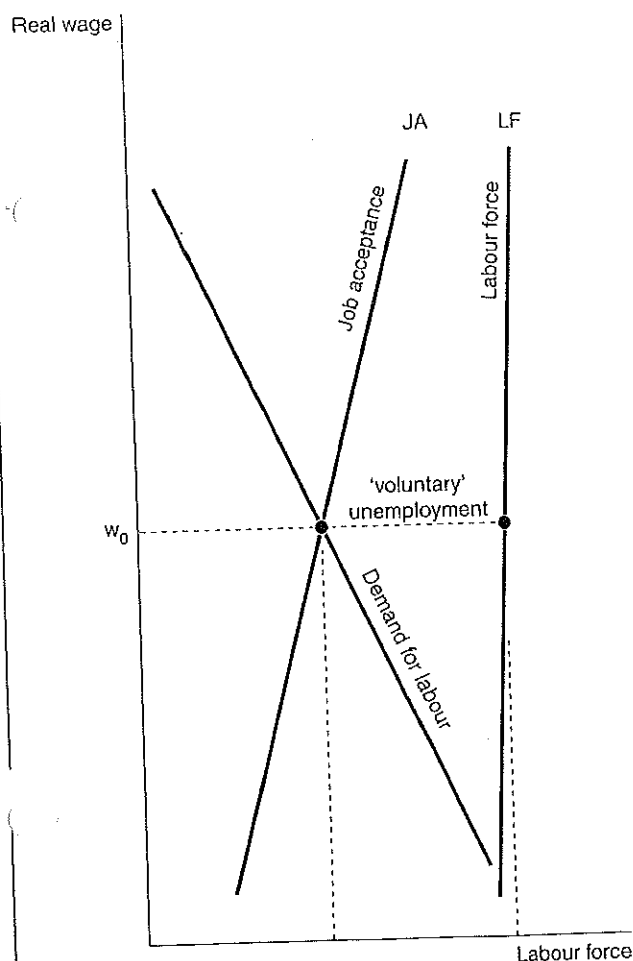
Unemployment continued

Monetarist and Keynesian views of unemployment

Monetarists believe that money wages and prices are flexible and adjust quickly, so that the real wage is at the right level to achieve long run equilibrium in the labour market, i.e. the labour market clears quickly and is either at or approaching full employment; all unemployment is 'voluntary'.

Keynesians believe money wages are slow to adjust (e.g. due to money illusion or contracts), and so the real wage may not adjust to clear the labour market, i.e. there can be 'involuntary' and 'voluntary' unemployment.

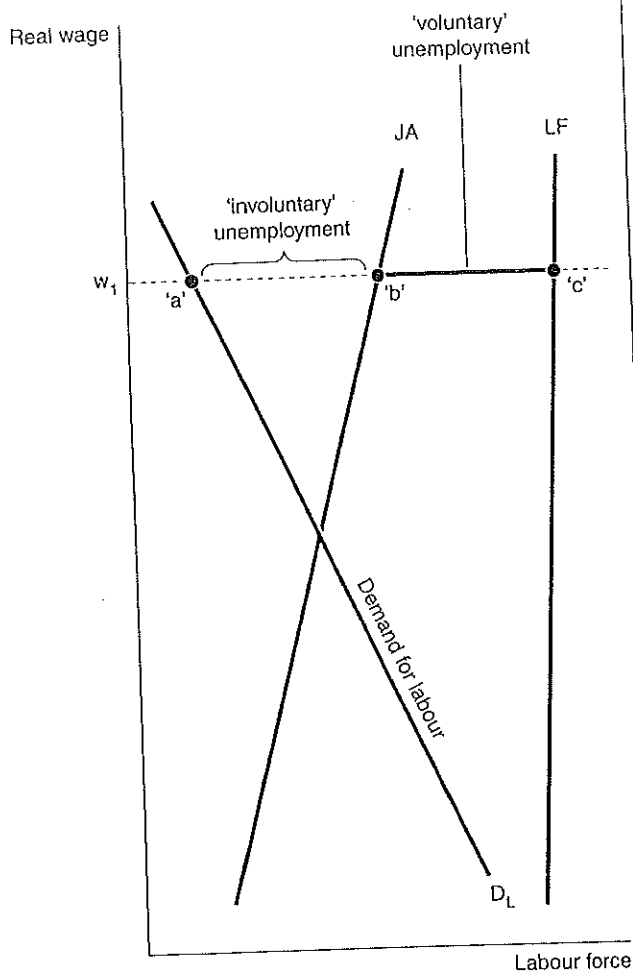
Imagine demand falls and inflation falls. If money wage growth falls as well, the real wage remains unchanged and the economy stays at full employment (monetarist). If money wage growth does not fall, the real wage has increased and there will be less labour demanded and there will be 'involuntary' unemployment in the short run until money wage growth does fall (Keynesian). The problem according to Keynesians is that the 'short run' can actually be quite a long time, which is why the Government should intervene.



Job acceptance = number of workers willing and able to accept a job at each real wage. As the real wage increases, so does the number of people willing to accept jobs.

Labour force = number of people registered for work; this will also increase at higher real wages as people come back into the labour force.

The difference between the number of people in the labour force and the number accepting a job is 'voluntary unemployment'.



At real wage w_1 there are 'c' people in the labour force; 'b' want to accept a job, so 'bc' is 'voluntary' unemployment; 'ab' is 'involuntary' unemployment - these people are willing and able to work but are not demanded at the higher real wage. This assumes the high real wage is caused by imperfections in the labour market, e.g. money illusion which prevents money wages changing quickly. If the real wage is above equilibrium because of union power, it could be argued that 'ab' is 'voluntary' - the unions have volunteered workers for unemployment. This is 'classical unemployment'.